

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
AARON AND ELOISE MAGIDOW)

Appearances:

For Appellants: Walter S. Weiss
Attorney at Law

For Respondent: John R. Akin
Counsel

O P I N I O N

This appeal is made pursuant to section 18593 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Aaron and Eloise **Magidow** against proposed assessments of additional personal income tax and penalties in the amounts and for the years as follows:

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<u>Appellant</u>	<u>Y e a r</u>	<u>Amount</u>	<u>Final y</u>
Aaron Magidow	1962	\$ 512.10	\$256.05
	1963	360.85	
Aaron and Eloise Magidow	1964	2,005.86	
	1966	871.35	
	1967	5,940.20	
	1968	1,532.50	
	1969	1,648.10	
	1971	2,768.87	138.44

Reference hereinafter to "appellant" will be to appellant Aaron Magidow. The deductions at issue were claimed in connection with his business, Montebello Meat Packing Company.

On June 4, 1971, respondent received notice from the Internal Revenue Service that certain federal adjustments had been made to appellant's taxable income for 1969. On the basis of this information, respondent issued a notice of proposed assessment on October 29, 1971, adjusting appellant's -income for 1969 as appropriate under California law. When appellant indicated that the federal matter was not final, respondent agreed to defer action until the federal determination was concluded.,

In late 1973, respondent learned that appellant had filed petitions with the tax court covering 1962, 1963, 1964, 1966, 1967, 1968, and 1969. Pursuant to respondent's request, appellant submitted the federal audit reports and federal notices of deficiency (dated March 15, 1973) covering these years. Respondent utilized this information to issue its own notices of proposed assessment on March 19, 1974, for the years 1962, 1963, 1964, 1966, 1967 and 1968. Pursuant to appellant's request, respondent also deferred further action on these matters since they too were not yet final at the federal, level.

On November 16, 1976, appellant settled the cases that were before the tax court, establishing his federal tax liability for all of those years, The corresponding tax court orders, entered on that same date, and copies of which appellant furnished to respondent, showed only appellant's adjusted tax liability. The exception was the order for 1964, which included audit information. Since audit information was necessary in order for respondent to conform to the final federal determination, respondent requested that appellant provide a copy of the supporting federal audit report. However, appellant only

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provided respondent with additional copies of the stipulated orders. In view of the absence of the needed audit information, respondent estimated the amounts of the federal adjustments-for all years except 1964 and used these estimates to reconstruct appellant's federal income. For 1964, the actual audit data was used. Conforming adjustments to appellants' California taxable income were then made for all the years at issue and corresponding notices of action were issued on February 27, 1978,

Respondent also received a separate notice from the Internal Revenue Service indicating that federal adjustments had been made to appellant's taxable income for 1971. Respondent accordingly issued, on October 21, 1977, a Notice of Additional Tax Proposed To Be Assessed, including a negligence penalty. Appellant informed respondent that the federal adjustments had been revised and submitted a copy of a tax court order and an audit report as evidence of the revisions. As a consequence, respondent issued a revised notice on February 27, 1978, incorporating the federal changes.

Appellant protested all the above proposed assessments. After due consideration of the protests, respondent upheld its proposed assessments, and this appeal followed. Subsequent to the filing of this appeal, respondent made certain concessions and corrections. Respondent has abated the penalty (fraud) for the year 1962. Respondent has also reduced certain of the proposed assessments due to computational errors. For 1967, the proposed assessment is reduced from \$5,940.20 to \$5,640.20; for 1959, the proposed assessment is reduced from \$1,648.10 to \$1,620.00; and for 1971, the proposed assessment is reduced from \$2,768.87 to \$2,745.32.

A preliminary question that has been raised with respect to all the proposed assessments under review is whether such proposed assessments are barred by the statute of limitations. The basic statute of limitations for deficiency assessments is contained in Revenue and Taxation Code section 18586, which provides:

Except in case of a fraudulent return and except as otherwise expressly provided in this part, every notice of a proposed deficiency assessment shall be mailed to the taxpayer within four years after the return was filed. No deficiency shall be assessed or collected with respect to the year for which the return was filed unless the notice is mailed within the four-year period or the period otherwise fixed,

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The notice of proposed deficiency assessment for 1969 was issued on October 29, 1971. That **particular** notice **fell** clearly within the basic four-year **limitations** period. As to the remaining notices of proposed assessment, further examination is necessary.

Section 18586 is a general statute of limitations and it expressly provides for **exceptions** to the general rule. Either of two exceptions applies when **federal changes** are made to a taxpayer's gross income or deductions, depending on whether or not the taxpayer reports the changes to the Franchise Tax Board in a timely fashion as required by section 18451 of the Revenue and Taxation Code,

Section 18451 provides in pertinent part as follows:

If **the** amount of **gross** income or deductions for any year of any taxpayer as returned to the United States **Treasury** Department is changed or corrected by the Commissioner of Internal Revenue or other officer of the United States or other competent authority, ... such taxpayer shall report such change or correction, ... within 90 days after the final determination of such change or correction ..., or as required by the Franchise Tax **Board**, and shall concede the accuracy of such determination or state wherein it is erroneous,

If the taxpayer complies with section 18451 by reporting federal tax changes within the required time period, the Franchise Tax Board has six months from the reporting date to mail a notice of proposed deficiency assessment (Rev. & Tax. Code, § 18586.3); if the taxpayer does not comply with section 18541, the Franchise Tax Board has four years from the date of the federal changes in which to mail such notice. (Rev. & Tax. Code, § 18586.2.)

The **above-noted** extensions of the basic tax deficiency statute of limitations commence either with the date of the final federal determination or at some time within 90 days of that date. In the instant matter, the notices of proposed deficiency assessment for 1962, 1963, 1964, 1966, 1967, and 1968 were **issued** on March 19, 1974. This was well before the date that the final federal determination took place, November 16, 1976. Under these circumstances, respondent's notices were obviously issued within the applicable limitations period. (Appeal of David B. and Delores Y. Gibson, Cal. St. Bd. of Equal., April 22, 1975; Appeal of King and Dorothy Crosno, et al., Cal. St. Bd. of Equal., January 9, 1979.)

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With respect to 1971, the date of the final federal determination is not certain since the tax court order concerning that year is undated. However, 'it is known that appellant filed his tax court petition for that year on April 13, 1976. It is further observed that part of the federal audit report for 1971 was completed on a form last revised in June of 1976. Given that the audit report was the basis for the settlement into which appellant entered with the Internal Revenue Service, it is our opinion that the final determination concerning appellant's federal tax liability for 1971 occurred after June of 1976. Appellant reported the final federal agreement to respondent on December 6, 1977. If appellant reported the change within 90 days of its occurrence, respondent had six months from December 6, 1977, in which to issue a proposed deficiency. If appellant did not report the change as required, respondent had four years from June of 1976, or later, in which to issue a **proposed** deficiency. **Respondent's** notice, issued on October 21, 1977, either preceded or was well within the applicable extension to the statute of limitations. It is therefore clear that respondent's notice of proposed deficiency assessment for 1971 was issued within the applicable limitations period specified by law.

The remaining issue in this appeal is whether appellant has shown that respondent's proposed deficiency assessments are erroneous. Appellant's contention that respondent's proposed assessments are in error is based on the further argument that the federal adjustments on which they are based are contrary to law. In making this argument, appellant has addressed himself to three particular items involved in the federal changes to his income tax liability.

The first of these relates to 1964 and the stipulated tax court order associated therewith specifying that appellant received constructive dividends in the amount of **\$22,936.13** for that year. Appellant concedes the receipt of constructive dividends. He contends, **however**, that as the sole shareholder of a corporation engaged in the meatpacking business, he incurred offsetting business expenses. He claims that he made payoffs to supermarket buyers so that such buyer-agents would purchase beef from appellant. Appellant declared that such payments were common in that particular line of business. The second item has to do with claimed business bad debt losses over several years in the total amount of **\$175,000.00**. These losses are said to have occurred when appellant, as a stockholder-guarantor, was required to make loan repayments on behalf of a corporation which was a buyer of meat products from Mo'ntebello Meat Packing Co. He contends that the business relationship between the two companies qualified the payments as business

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bad debts. The last item involves a claimed interest expense of \$22,000.00 in 1971. Appellant claims that he paid a 10 percent charge to a business associate for guaranteeing appellant's \$220,000.00 bank loan. He characterizes this "fee" as additional interest over and above the interest paid to the bank for the loan itself.

Appellant has not, however, presented any evidence to corroborate any of his assertions. There is no proof that he actually made any of these alleged payments. Since a deficiency assessment based on a federal audit report is presumptively correct (see Rev. & Tax. Code, § 18451, quoted above), and the taxpayer bears the burden of proving that respondent's determination is erroneous (Appeal of Vera Ralston Yates, Cal. St. Bd. of Equal., March 30, 1981; Appeal of Donald G. and Franceen Webb, Cal. St. Bd. of Equal., Aug. 19, 1975; Appeal of Nicholas H. Obritsch, Cal. St. Bd. of Equal., Feb. 17, 1959), it is our view that appellant's unsupported assertions are not sufficient to satisfy that burden. Appellant has therefore failed to show any error with respect to the three challenged items. For that matter, none of the other federal adjustments has been shown to be incorrect, including the negligence penalty for 1971. Since respondent's imposition of a negligence penalty based on a similar federal penalty is entitled to a presumption of correctness (Appeal of Ruth Wertheim Smith, Cal. St. Bd. of Equal., Aug. 3, 1965; Appeal of Casper W. and Svea Smith, Cal. St. Bd. of Equal., April 5, 1976), and since nothing in appellant's presentation indicates that this penalty is incorrect, it also must stand.

Finally, it is noted that appellants have objected to the imposition of interest. There is no merit to this objection since section 18688 of the Revenue and Taxation Code mandates the imposition of interest in such matters. Moreover, the imposition of interest is but the compensation for the taxpayer's use of the money. (Appeal of Patrick J. and Brenda T. Harrington, Cal. St. Bd. of Equal., Jan. 11, 1978.)

For the reasons stated above, we conclude that all of respondent's actions must be upheld, subject to the concessions to which reference was made above.

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O R D E R

Pursuant to the views **expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,**

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of Aaron and Eloise **Magidow** against proposed assessments of personal income tax and penalties in the amounts and for the years set forth below, be and the same is hereby modified in accordance with respondent's concessions. In all other respects, the action of the Franchise Tax Board is sustained.

<u>Appellant</u>	<u>Year</u>	<u>Amount</u>	<u>Penalty</u>
Aaron Magidow	1962	\$ 512.10	\$256.05
	1963	360.85	
Aaron and Eloise Magidow	1964	2,005.86	
	1966	871.35	
	1967	5,940.20	
	1968	1,532.50	
	1969	1,648.10	
	1971	2,768.87	138.44

Done at Sacramento, California, this 17th day of November , 1982, by the State Board of Equalization, with Board **Members** Mr. Bennett, Mr. **Collis**, Mr. Dronenburg and Mr. Nevins present.

William M. Bennett , Chairman
Conway H. Collis , Member
Ernest J. Drone-nburg, Jr. , Member
Richard Nevins , Member
_____, Member